

ORIGINAL DOCKET FILE COPY **RECEIVED**
Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554
SEP 4 - 1998

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
)
1998 Biennial Regulatory Review --) CC Docket No. 98-117
Review of ARMIS Reporting Requirements)
)

MCI REPLY COMMENTS

MCI Telecommunications Corporation (MCI) hereby submits its reply to comments on the Notice of Proposed Rulemaking in the above-captioned docket.¹

The Commission should not adopt the ILECs' proposals because they would impair the ability of the Commission and interested parties to monitor the ILECs' cost allocation processes and to obtain cost information currently used in a wide range of regulatory settings. For the reasons discussed below, the Commission should, at a minimum, maintain the level of reporting detail concerning ILEC costs and cost allocation processes that is captured by the existing ARMIS reports.

I. The Scope of the Notice Proposals is Consistent with Section 11 of the Act

The large ILECs argue that Section 11(a)(1) of the Act requires much broader revisions to the ARMIS reports than the Commission is proposing in the Notice. Bell Atlantic, for example, argues that Section 11 "requires the Commission to review all of its regulations every two years" and to repeal any regulation it determines to be no longer "necessary."² Bell

¹1998 Biennial Regulatory Review -- Review of ARMIS Reporting Requirements, CC Docket No. 98-117, FCC 98-147, released July 17, 1998 (Notice).

²Bell Atlantic Comments at 1-2 (emphasis in original).
No. of Copies rec'd
List ABCDE

0x6

Atlantic asserts that the Notice “clearly fails to meet these exacting legal standards.”³ Bell Atlantic also claims that the “substantial costs” of preparing the ARMIS reports “cannot be justified unless the Commission can show that the data in the ARMIS reports are necessary to carry out the Commission’s new functions under the Telecommunications Act of 1996.”⁴

As MCI discusses in its reply comments in the companion CC Docket No. 98-81 accounting review proceeding, the ILECs misread Section 11 of the Act.⁵ While Section 11(a)(1) of the Act requires the Commission to review “all regulations issued under this Act,” the ILECs are ignoring Section 11(a)(2), which obliges the Commission to repeal or modify only those rules no longer necessary as the result of “meaningful economic competition” between providers of telecommunications services.

Application of the “meaningful economic competition” standard shows that the limited scope of the Commission’s proposals is fully consistent with Section 11 of the Act. As the Commission is well aware, there has been little or no change in the level of competition for ILEC local exchange and exchange access services since the passage of the Telecommunications Act of 1996. The ILECs have certainly presented no evidence in this proceeding that would allow the Commission to conclude that meaningful economic competition exists. Consequently, nothing in Section 11 obliges the Commission to repeal or modify any of the rules that it has adopted to ensure that rates are just and reasonable, including the ARMIS filing requirement and ARMIS reports themselves.

³Id. at 2.

⁴Id. at 6.

⁵MCI Reply Comments, CC Docket No. 98-81, September 4, 1998, at .

Furthermore, in the Joint Cost Order, the LEC Price Cap Order, and several other proceedings, a critical factor in the policy determinations made by the Commission was that ARMIS reporting would be available to monitor the effectiveness of the adopted rules. For example, in the LEC Price Cap Order the Commission “reviewed [its] monitoring and data collection capabilities and requirements . . . to ensure that they provide information that is accurate and sufficient to this task [of conducting performance reviews of the price cap plan].”⁶ As long as the rules adopted in these orders remain in force, the Commission cannot simply eliminate one of the foundations on which its policy determinations were based. The ILECs’ attack on the ARMIS reporting requirements is in effect an attack on a broad range of Commission rules.

The alleged “burden” of complying with the ARMIS filing requirements is irrelevant to the Commission’s analysis under Section 11 of the Act. Section 11 requires only that the Commission assess whether a regulation is no longer necessary as a result of meaningful economic competition. Once the Commission has determined that meaningful economic competition has not developed, nothing in Section 11 requires the Commission to conduct a cost-benefit analysis or otherwise revisit the reasoning underlying each of its rules. In any event, as AT&T points out, the Commission only recently found again that “for carriers with annual revenues in excess of [the \$112 million] threshold . . . , the benefits [of ARMIS

⁶LEC Price Cap Order, 5 FCC Rcd at 6832-6833.

reporting] to ratepayers outweigh the cost to those carriers of requiring compliance.”⁷ There is no reasoned basis for the Commission to change course at this time.⁸

Moreover, the ILECs’ own figures show that the “burden” of filing ARMIS reports is minimal. Bell Atlantic, for example, calculates the cost of compiling and filing its ARMIS reports to be only \$1 million per year,⁹ while Ameritech cites ARMIS filing costs of only \$1.7 million per year.¹⁰ Given that Bell Atlantic had operating telephone company revenues of \$24.9 billion in 1997,¹¹ an expenditure of \$1 million, or 0.004 percent of revenues, can be considered a trivial cost burden.

II. The Commission Should Not Adopt the ILECs’ Proposed Revisions to the ARMIS Financial Reports

Several ILECs present proposals for sweeping changes to the ARMIS 43-01, 43-02, 43-03, and 43-04 financial reports. The ILECs justify this substantial reduction in the level of reporting detail on the grounds that accounting costs are no longer relevant under price cap regulation. BellSouth contends, for example, that “[t]he price regulation paradigm breaks the link between accounting costs and rates, thereby eliminating the need to require such detailed

⁷AT&T Comments at 6 (citing Implementation of the Telecommunications Act of 1996: Reform of Filing Requirements and Carrier Classifications, Report and Order, 12 FCC Rcd 8071, 8103 (1997) (Reform of Filing Requirements Order)).

⁸See, e.g., *Motor Vehicle Manufacturers Association v. State Farm Automobile Insurance Company*, 463 U.S. 29, 41-4.

⁹Bell Atlantic Comments at 5.

¹⁰Ameritech Comments at 4.

¹¹1997 Preliminary Statistics of Common Carriers, Table 1.2.

ARMIS reports that large ILECs are currently required to file.”¹² Bell Atlantic and USTA argue that, to the extent that accounting costs are still used under price cap regulation, such as in computing exogenous cost changes and forecasting the base factor portion, the cost information can be submitted on an as-needed basis as part of the tariff filing.¹³

A. Reporting of Financial Information Is Still Necessary Under Price Cap Regulation

As MCI demonstrates in its Reply Comments filed today in the CC Docket No. 98-81 accounting review proceeding, the ILECs are incorrect when they argue that accounting costs are no longer relevant. Reported earnings are used by the Commission and state regulators to assess the reasonableness of price cap or incentive regulation plans, and 18 states and the District of Columbia still use rate of return regulation. Moreover, under the Commission’s price cap plan, accounting costs are used in several ways: to determine low-end adjustments, evaluate above-cap tariff filings, calculate exogenous costs, develop the subscriber line charge, and derive inputs for new services cost studies.

As long as accounting costs still play a key role in ensuring that rates are just and reasonable, the original purpose of the ARMIS financial reports -- “to facilitate the timely and efficient analysis of revenue requirements and rates of return, to provide an improved basis for audit and other oversight functions, and to enhance [the Commission’s] ability to quantify the effects of alternative policy proposals” -- remains valid.¹⁴ Indeed, as AT&T points out, the

¹²BellSouth Comments at 4.

¹³USTA Comments at 4; Bell Atlantic Comments at 3.

¹⁴In the Matter of Automated Reporting Requirements for Certain Class A and Tier 1 Telephone Companies, Report and Order, 2 FCC Rcd 5770 (1987) (ARMIS Order).

Commission reiterated only a year ago that cost information from ARMIS reports “has also played an important role in tariff investigations, certain rulemakings concerning cost issues, and in the evaluation of exogenous cost adjustments under the price cap rules.”¹⁵

In many ways, the scope of application of the ARMIS financial reports has expanded since the passage of the Telecommunications Act of 1996. Cost information reported in ARMIS has been used to compute wholesale discounts and to determine unbundled network element (UNE) and interconnection prices.¹⁶ While the methodologies used for much of the costing of UNEs and interconnection under the 1996 Act is forward-looking and does not rely explicitly on historical accounting data, the models used in this costing often employ factors such as expense to investment ratios that are derived from cost information reported in ARMIS.¹⁷

The Commission should reject USTA and Bell Atlantic’s argument that cost data presented on an as-needed basis in tariff filings is sufficient. First, as discussed above, ARMIS data is used for a variety of purposes unrelated to tariff filings. Second, in the context of tariff filings, it is clear that cost support presented on an ad hoc basis is not sufficient. In fact, ARMIS data is routinely used by the Commission and interested parties to evaluate and challenge the reasonableness of tariff cost support. For example, ARMIS data has been used by

¹⁵AT&T Comments at 6 (citing Reform of Filing Requirements Order, 12 FCC Rcd at 8098 n.135.

¹⁶In the Matter of Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, rel. August 8, 1998, at ¶¶898-906, 917-918.

¹⁷See GTE Telephone Operating Companies: Release of Information Obtained During Joint Audit, Memorandum Opinion and Order, AAD 98-26, released March 18, 1998, at ¶6.

the Commission to evaluate the “overhead loading factor” that ILECs apply in new services cost justifications.¹⁸ ARMIS data is also used on a regular basis to challenge the price cap ILECs’ exogenous cost calculations or base factor portion (BFP) forecasts. Less than a year ago, the Commission used ARMIS data to find that the exogenous cost changes and base factor portion forecasts that several price cap ILECs had filed with their 1997 annual access filings were not just and reasonable.¹⁹

B. ILEC Proposals

The Commission should not adopt the ILECs’ proposals for revising the ARMIS report formats. With minor exceptions, the current level of detail provided by the ARMIS reports remains necessary to the Commission’s regulatory objectives. The Commission should, in particular, continue to require the ILECs to report information at the Class A account level of detail. As MCI discussed in its initial comments, Class A detail serves a variety of key regulatory purposes, including monitoring of regulated/nonregulated allocations and deriving cost factors for use in new services cost studies and forward-looking cost models.²⁰

The Commission should also continue to require ILECs to provide cost information sufficient for the Commission and interested parties to trace the ILECs’ cost allocation processes. The reported costs that are used by the Commission and the states in regulating ILEC rates are the end product of a series of cost allocation processes: the Part 64

¹⁸In the Matter of Ameritech Operating Companies Revisions to Tariff F.C.C. No. 2, Transmittal Nos. 697, 711, Order, 8 FCC Rcd 4589, ¶¶32-37 (1993).

¹⁹In the Matter of 1997 Annual Access Tariff Filings, Memorandum Opinion and Order, CC Docket No. 97-149, rel. December 1, 1997, at ¶¶15, ¶¶137-151.

²⁰MCI Comments, CC Docket No. 98-117, pp.3-4.

regulated/nonregulated allocation, the Part 36 separations process, and the Part 69 cost allocation. The current ARMIS report formats permit the Commission and interested parties to trace each ILEC's cost allocation process from Part 32 accounts to Part 69 elements, at a level of detail sufficient for the Commission and interested parties to evaluate whether the cost allocations appear to be consistent with the Commission's rules. The ILECs' proposals, by contrast, would obscure several key aspects of the cost allocation process.

First, the ILECs' proposals would reduce substantially the level of reporting detail concerning the Part 64 regulated/nonregulated cost allocation process. Under the ILECs' proposals, the ILECs would report only the results of the cost allocation process -- the regulated/nonregulated split -- and only report this data at the Class B level of accounts. The present ARMIS 43-03 report, on the other hand, shows not only the overall regulated/nonregulated breakdown but also the amounts allocated using each of the Part 64 cost allocation methods. As MCI discussed in its initial comments, this detail permits the Commission to monitor whether the ILEC has used direct assignment whenever possible, as is required by the Joint Cost Order.²¹

Second, the ILECs' proposals would significantly reduce the Commission and the states' ability to trace the separation of costs between the interstate and intrastate jurisdictions. Under the ILECs' proposals, the ILECs would report only the end result of the separations process -- the interstate/intrastate breakdown -- and a selection of separations factors. The Commission and interested parties would not be able to see (1) the underlying data used to

²¹MCI Comments at 6-7 (citing Joint Cost Order, 2 FCC Rcd at 1318).

derive the separations factors, as is shown on the 43-04 report;²² (2) the allocation of costs between separations categories;²³ and (3) interstate and intrastate assignments of costs allocated using direct assignment.²⁴ In sum, the Commission and interested parties would not be provided with the same step-by-step description of the ILEC's separations process that is currently shown on the 43-04 report. This would make it significantly more difficult for the Commission and interested parties to monitor the ILECs' compliance with the separations rules, and also make it significantly more difficult for the Commission to evaluate changes to the separations process.

Third, the ILECs' proposals would significantly limit the Part 69 information provided to the Commission. USTA would almost eliminate Part 69 information entirely; its proposed report format would require the ILECs to report only three categories: interexchange, access, and billing and collection. SBC would require the ILECs to report only a total traffic sensitive figure, not separate switching, transport, and information. The Commission should not adopt these proposals. The present ARMIS 43-01 and 43-04 reports provide Part 69 cost allocation detail that is required for verifying basket-by-basket exogenous cost changes proposed by the ILECs, or to obtain service-specific cost factors.

Fourth, USTA is proposing to eliminate a variety of other reports and schedules that provide key information concerning ILEC activities. For example, despite the Commission's recent finding that affiliate transactions continue to present opportunities for cost shifting,

²²See, e.g., ARMIS 43-04, row 1216.

²³See, e.g., ARMIS 43-04, rows 1220-1222.

²⁴See, e.g., ARMIS 43-04, row 1220.

USTA would eliminate those the ARMIS 43-02 Table B-3 "Investments in Affiliates," Table B-4, "Analysis of Assets Purchased or Sold to Affiliates," and Table I-2, "Analysis of Services Purchased From or Sold to Affiliates." USTA would also eliminate all ARMIS 43-02 tables that provide depreciation information. As AT&T points out, however, these tables assist the Commission and interested parties in reviewing the appropriateness of LEC's accumulated depreciation and depreciation expense.²⁵

The Commission should not make the sweeping changes that the ILECs propose. The ILECs' proposals would, without question, obscure the trail of cost allocations and limit the Commission's ability to ensure compliance with its accounting rules. At most, the Commission should make limited and targeted revisions to its ARMIS reporting rules such as the elimination of the payphone column on the ARMIS 43-01 and 43-04 reports, as suggested in the Notice.

IV. Conclusion

For the reasons discussed herein and in MCI's initial comments, the Commission should not adopt the ILECs' proposals for revisions to the ARMIS report formats. The Commission should, at a minimum, maintain the current level of reporting detail concerning ILEC costs and cost allocation processes.

Respectfully submitted,
MCI TELECOMMUNICATIONS CORPORATION




Alan Buzacott
1801 Pennsylvania Ave., NW
Washington, DC 20006
(202) 887-3204

September 4, 1998

²⁵AT&T Comments at 3 n.3.

STATEMENT OF VERIFICATION

I have read the foregoing, and to the best of my knowledge, information, and belief there is good ground to support it, and that it is not interposed for delay. I verify under penalty of perjury that the foregoing is true and correct. Executed on September 4, 1998.



Alan Buzacott
Regulatory Analyst
1801 Pennsylvania Ave. NW
Washington, D.C. 20006
(202) 887-3204

CERTIFICATE OF SERVICE

I, Vivian I. Lee, do hereby certify that copies of the foregoing Reply Comments were sent via first class mail, postage paid, to the following on this 4th day of September, 1998.

International Transcription Services**
1231 20th Street, N.W.,
Washington, DC 20036

Anthony Dale
Accounting Safeguards Division
Common Carrier Bureau
FCC
2000 L Street, Suite 201
Washington, DC 20036

Robert M. Lynch
Durward D. Dupre
Darryl W. Howard
Jonathan W. Royston
SWBT
One Bell Plaza, Room 3022
Dallas, TX 75202

M. Robert Sutherland
Stephen L. Earnest
BellSouth Corporation
Suite 1700
1155 Peachtree Street, N.W.
Atlanta, GA 30309-3610

Joseph DiBella
Bell Atlantic
1320 N. Court House Road
8th Floor
Arlington, VA 22201

Nancy Rue
Attorney for Cincinnati Bell Telephone
Company
Frost & Jacobs LLP
2500 PNC Center

201 East Fifth Street
Cincinnati, OH 45202

Michael J. Shortley, III
Frontier
180 South Clinton Avenue
Rochester, NY 14646

David W. Zesiger
ITTA
1300 Connecticut Avenue, Suite 600
Washington, DC 20036

Leander R. Valent
Ameritech
9525 West Bryn Mawr, Suite 600
Rosemont, IL 60018

Carolyn C. Hill
Alltel
655 15th Street, N.W.
Suite 220
Washington, DC 20005

Mark C. Rosenblum
Judy Sello
AT&T
Room 3245I1
295 North Maple Avenue
Basking Ridge, NJ 07920

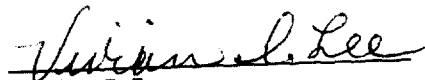
James T. Hannon
U S West, Inc.
Suite 700
1020 19th Street, N.W.
Washington, DC 20036

Emily C. Hewitt
George N. Barclay
Michael J. Ettner
GSA
1800 F Street, N.W., Room 4002
Washington, DC 20405

Jay C. Keithley
Sprint LTCs
1850 M Street, N.W., 11th Floor
Washington, DC 20036-5807

Lawrence E. Sarjeant
Linda L. Kent
Keith Townsend
John W. Hunter
1401 H Street, N.W., Suite 600
Washington, DC 20005

****HAND DELIVERED**


Vivian I. Lee